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ANNUAL REPORT

OF

MARSHALL FIELD & COMPANY

YEAR ENDED
DECEMBER 31, 1938

BOARDS
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CORPORATE OFFICES

The Merchandise Mart
222 North Bank Drive : Chicago, Illinois

MRB
CORP. FILE

MARSHALL FIELD & COMPANY

BOARD OF DIRECTORS

FREDERICK D. CORLEY
MARSHALL FIELD
STANLEY FIELD
HUGHSTON M. McBAIN
CHARLES H. SCHWEPPE
JAMES SIMPSON
JAMES SIMPSON, JR.
ALBERT A. SPRAGUE
JOHN P. WILSON

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FREDERICK D. CORLEY

First Vice-President
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Vice-Presidents
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Secretary-Treasurer
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Comptroller
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Assistant Comptroller
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Assistant Treasurer
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Assistant Comptroller
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CHICAGO
GUARANTY TRUST COMPANY OF NEW YORK
NEW YORK

Registrars
THE FIRST NATIONAL BANK OF CHICAGO
CHICAGO
BANKERS TRUST COMPANY
NEW YORK

TO THE STOCKHOLDERS:

The Board of Directors submits this annual report for the year ended December 31, 1938.

Our 1938 operating results show an improvement over those of 1937, and we are particularly gratified that every division of the business made a net profit for the year. The comparative results of the two years are as follows:

	1938	1937
Retail Division	$3,940,099	$5,029,090
Manufacturing Division	138,165	*5,679,209**
Real Estate Division	209,968	*25,297**
Profit or loss from operations before interest and special charges	$4,288,232	*$ 675,416**
DEDUCT —		
Interest charges	$ 612,257	$ 665,105
Special compensation under stock option agreement	33,737	313,930
Provision for Federal income tax (See Note 3 on page 10)	150,000	—
	$ 795,994	$ 979,035
Net profit or loss for year	$3,492,238	*$1,654,451**

(**Indicates a loss*)

The results of operations shown above are after provisions for depreciation of buildings, machinery and equipment, and the amortization of leaseholds, of $2,349,332 in 1938 and $2,421,375 in 1937.

1938 earnings, after provision for all dividend requirements on both classes of preferred stock, including dividends accrued but unpaid, are equivalent to approximately $1.04 per share on the net number of 1,644,057 shares of no par value common stock outstanding.

Merchandise sales and real estate income were as follows:

1937	$100,044,813
1938	82,279,916
Decrease	$ 17,764,897

Sales of lines discontinued during the year are not included in the 1938 sales figure shown above, but were handled through a reserve account referred to on page 4. If 1937 sales of such lines are eliminated from the 1937 sales figure, the 1938 decrease would be $7,280,789, or 8.1%.

RETAIL DIVISION

During the year no changes were made in the number of units comprising our Retail Division, which consists of our Retail Store, State Street, Chicago; suburban stores in Evanston, Oak Park, and Lake Forest, Illinois; Frederick & Nelson, Seattle, Washington; and two small stores, one located at Chicago Heights, Illinois, and the other at Watertown, South Dakota.

The 1938 net profit of the Retail Division showed a decrease from the previous year, due to a 6% lower volume of sales, a small reduction in gross profit percentage, and a slight increase in our expense percentage.

The lower sales volume was largely accounted for by a decline in the index of retail prices, which adversely affected the size of the average sales check. We found that business was difficult to obtain during the early part of the year, but it improved during the latter half year, and in December the dollar volume of the Main Retail Store and of our seven retail stores was greater than in December of any of the preceding seven years.

Controllable expenses were considerably reduced, but non-controllable expenses, including taxes, were higher than in the previous year. A greater number of transactions made it impossible to reduce expenses proportionately with the decline in dollar volume, as only slightly fewer employes were required to serve customers.

We handled more sales transactions during 1938 than in the previous year, and during the Christmas season the number of transactions was the largest in the history of the Chicago and suburban stores. These stores mailed more statements to customers during the year and for the month of December than for any comparable periods in the past. The continued upward trend in this respect is encouraging.

Our stocks of merchandise and our accounts receivable are in sound condition. At the year end our inventories were lower than at the end of 1937 or 1936, while our collections were good throughout the year and adequate reserves are maintained against possible losses on credit sales.

A number of physical changes and improvements were made during the year in the various retail stores, in order to make them more modern, attractive, and convenient to customers, and we expect to continue our traditions in this respect.

A start was made on Chicago's subway during 1938, and we believe that the completion of this long needed improvement will be beneficial to us and to Chicago business generally. We have been advised that our State Street building foundations are such as to make unnecessary any large expenditures for protection of the property in connection with subway construction.

MANUFACTURING DIVISION

The reorganization and the elimination of certain lines in the Manufacturing Division, covered in our last annual report, have now been completed. As planned, we discontinued a number of departments which had not shown consistent profits over a period of years. The departments so discontinued handled the following lines of merchandise, none of which we plan to manufacture, convert, or job in the future: cotton dress goods, draperies, gloves, handkerchiefs, knitted undergarments, linens, plush, silk piece goods, cotton, silk and rayon lingerie, wash dresses, and Wilton rugs. These departments formerly accounted for approximately $10,500,000 of our total net sales. In this connection, operations in three small domestic mills and in the Philippine Islands, China, and Puerto Rico were discontinued.

As of December 31, 1937 there was a reserve of $3,569,682 on our books to provide for losses anticipated in the process of eliminating these activities, and during the year losses of $2,423,524 sustained on the disposition of inventories and properties were charged to this reserve.

Incident thereto, a considerable amount of space held under long-term leases was vacated and sublet at rentals which will result in losses over the terms of the leases. To cover this contingency an amount of $886,406 was transferred from the reserve described above and added to the reserve for loss on subleases, which at the year end amounted to $1,175,659 and is considered adequate for this purpose.

No losses or expenses other than those directly incurred in the elimination of the above merchandise lines were charged to the reserve. As the merchandise liquidation operation was entirely completed, the excess of $259,752 was restored to earned surplus, and the reserve account was closed. All of the above adjustments are shown in the statements of surplus and reserve accounts on pages 10 and 11.

The Manufacturing Division now consists of twelve mills, eleven of which are located in North Carolina and Virginia and the twelfth at Zion, Illinois. We have no plans for disposing of any of these properties, and believe that they can be operated with satisfactory results in the future, as they have been in many prior years. These mills represent a large and important business, employing over 5700 people at the year end.

We are now manufacturing blankets, sheets, bedspreads, towels, Karastan Rug Mill products, and Zion lace curtains, and distributing them through our own sales organization to retail stores and jobbers throughout the country. We are also manufacturing woolen piece goods, rayon and silk gray goods, cotton and rayon suitings, and women's silk hosiery, and distributing these products through various selling agencies, which we have found to be more economical and satisfactory than distribution through our own sales organization. We plan to continue these operations on the present basis.

During the year large reductions were made in administrative, overhead and selling expenses. Beginning at mid-year, textile activity improved materially over the low and unsatisfactory level maintained throughout the spring selling season.

A conservative inventory policy was followed throughout the year, and we avoided the drastic losses experienced in the previous year caused by the price decline in cotton, silk, and wool. In this connection, cotton hedging was successfully employed, and we anticipated our raw material requirements to a lesser extent.

Manufacturing Division inventories of a year ago have been substantially reduced, and including raw materials and work in process, totaled $3,264,033 as of December 31, 1938, as compared with $10,410,292 at the close of the preceding year. Most of this reduction is applicable to the lines discontinued during 1938.

At December 31, 1938, our future commitments for raw materials were considerably lower than at the beginning of the year. We believe that our commitments are in no way excessive or beyond our normal requirements.

REAL ESTATE DIVISION

The Real Estate Division consists of The Merchandise Mart, and the "Annex" Office Building at Wabash Avenue and Washington Street, Chicago.

The operating results of The Merchandise Mart were primarily responsible for the improved showing of the Real Estate Division. At the end of the year The Mart was over 80% leased, an improvement over the situation a year earlier. Over 70% was occupied by outside tenants and under 10% by the company, which maintains its general Corporate Offices in the building, as well as showrooms for all of its manufactured lines and storage space for certain Retail Division merchandise.

The Mart's gross income was increased 12% in a year which presented many difficulites in the real estate field. Through operating economies a substantial part of this increase was carried through to net profit account.

During the year considerable unfinished space was converted into finished areas for new tenants. Notable among such areas are those on the seventh floor, where an attractive permanent building materials exhibit has been installed, and on the first floor, where we found it necessary to expand the main lobby and install eight new retail shop spaces, which will be ready for occupancy early in 1939.

The working population of The Mart has continued to increase, and a recent estimate indicates that our 747 tenants at the year end employed between 26,000 and 27,000 people.

A number of successful market events were held during the year, and we estimate that over 280,000 buying visits were made to the building during 1938. The market

events of early 1939 were the most successful in the history of the building, and spot checks of sales by representative tenants showed a gratifying increase in the amount of all kinds of goods sold.

During the year new leases for 308,715 square feet of space were signed, resulting in a net increase of 44 tenants and 153,650 square feet of rented area.

The "Annex" Office Building, which also houses our Store for Men, showed a further improvement in operating results over 1937, and should continue to contribute profitably to the Real Estate Division.

FINANCIAL MATTERS

Notwithstanding payment during the year of our $4,000,000 serial bank loan due from 1938 to 1941 inclusive, our cash position improved from $2,225,868 to $9,623,954 (the latter figure including $6,183,125 of short term United States Treasury Notes). This improvement resulted largely from the reduction of inventories and accounts receivable. At December 31, 1938, cash and its equivalent was almost $3,000,000 in excess of all current liabilities, and during the year our ratio of current assets to current liabilities improved to 4.9 to 1 from 3.9 to 1.

As stated in our last annual report, 1937 interest charges were approximately $470,000 less than those of 1936. As a result of the retirement of the serial bank loan, our interest charges will be further reduced by almost $100,000 per annum.

We have no maturities of funded debt to meet until 1942, when the first $1,000,000 of annual installments of our $14,000,000 first mortgage serial bond issue becomes due. In this connection, it is interesting to note that funded debt has been steadily reduced from its high point of over $32,000,000 in 1930 to the present $14,000,000 amount.

During the year, preferred dividends of $446,526 were paid, covering the first quarter's requirement on both the prior preferred and 6% cumulative preferred stock issues. At December 31, 1938, there remained $1,339,579 of preferred dividends unpaid and accrued.

Taxes continue to be a problem. For the year 1938 our tax expense of approximately $4,000,000 amounted to about five cents of every dollar of net merchandise sales, $13.32 per share of preferred stock of both classes, or $2.40 per share of common stock.

At the time of Mr. James O. McKinsey's death, his employment contract with us provided that his Estate might, on or before December 31, 1938, purchase 10,000 shares of unissued common stock at $10 a share, or receive a sum of money equal to the amount by which the market price (as defined in the contract) of such 10,000 shares exceeded $10 per share. On November 29, 1938 the Estate of Mr. McKinsey elected to take cash, with the result that an additional $33,737 was added to the $300,000 which

remains credited to his Estate on our books. This credit balance of $333,737 is held subject to the outcome of two pending law suits which raise certain questions concerning this contract.

The business formerly transacted by subsidiary corporations was transferred to the parent corporation during the year, and all subsidiaries have now become inactive. The financial statements contained in this report consequently cover the operations of the parent corporation alone and are not consolidated, as in former years.

PERSONNEL

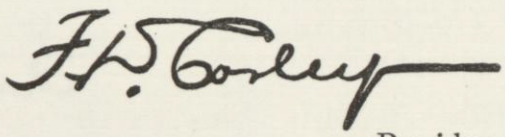
At the last annual stockholders' meeting, held April 8, 1938, Col. Albert A. Sprague and Mr. Hughston M. McBain were elected directors of the company. There have been no changes in the senior officers since our last annual report.

Mr. James L. Palmer, Director of Sales Promotion for the Chicago and suburban retail stores, was recently appointed Assistant to the President. Mr. Gerald A. Sivage was elected Assistant Treasurer. Mr. John C. Goodall, formerly Assistant Treasurer, was made Assistant to Vice-President Percy Wilson. Mr. Wilbur C. Munnecke, formerly Assistant Treasurer, was made Retail Operating Manager. The services of Mr. W. S. Street were secured as Assistant General Manager and Merchandise Manager of Frederick & Nelson.

The results obtained in 1938 would have been impossible without the wholehearted support of our fine organization, of which we are justly proud. Their welfare and advancement are constantly in our minds, and we intend to continue our present policy of promotion from our own ranks.

The directors are grateful to our 8000 stockholders and to our customers for their loyal support and cooperation during this past year, and look forward with confidence to a continuation of profitable operations.

By order of the Board of Directors,



President

February 8, 1939.

BALANCE SHEET—

ASSETS

CURRENT ASSETS:			
Cash and marketable securities—			
Cash in banks and on hand	$ 3,440,829		
U. S. Treasury Notes due in 1941, 1942, and 1943, at the lower of cost or market	6,183,125	$ 9,623,954	
Receivables—			
Accounts receivable from customers	$10,611,582		
Rents, claims, and miscellaneous receivables	413,806		
	$11,025,388		
Less—Reserve for doubtful accounts, etc.	496,177	10,529,211	
Merchandise inventories; quantities and condition determined by the company; priced at the lower of cost or market—			
Manufacturing Division merchandise, including raw materials and work in process of $1,773,300	$ 3,264,033		
Retail Division merchandise	9,417,036	12,681,069	
TOTAL CURRENT ASSETS			$32,834,234
PREPAID INSURANCE, SUPPLY INVENTORIES, ETC.			686,289
INVESTMENT SECURITIES, ETC.:			
Securities and cash deposited under construction agreements		$ 160,521	
Miscellaneous investments, receivables, etc.		178,326	338,847

FIXED ASSETS: Classification	Cost	Reserves for Depreciation and Amortization	Net	
Retail and manufacturing properties, etc.—				
Land	$ 874,543	$ —	$ 874,543	
Leaseholds	1,375,406	264,414	1,110,992	
Buildings and building equipment—				
On owned land	8,349,736	5,548,144	2,801,592	
On leased land	14,740,231	4,806,563	9,933,668	
Equipment	13,233,663	7,758,752	5,474,911	
Merchandise Mart (pledged under first mortgage)—				
Air rights and land	2,907,462	—	2,907,462	
Building and equipment	27,787,411	5,428,019	22,359,392	
TOTAL FIXED ASSETS	$69,268,452	$23,805,892	$45,462,560	45,462,560
GOODWILL, TRADE-MARKS, ETC.				1
				$79,321,931

NOTE No. 1.—Contingent Liabilities, etc.
Under letters of credit and guaranties—$275,000.
Under long-term leases—rentals payable are at present approximately $1,200,000 per year.

& COMPANY

DECEMBER 31, 1938

LIABILITIES

Current Liabilities:			
Accounts payable—			
Trade creditors	$ 2,318,452		
Customers' credit balances and sundry accounts payable	361,110	$ 2,679,562	
Liability to Estate of James O. McKinsey under options exercised in 1937 and 1938		333,737	
Accruals—			
Salaries and wages	$ 870,973		
Local and miscellaneous taxes	2,296,346		
Other accrued expenses	308,684		
Federal income tax	170,000	3,646,003	
Total Current Liabilities			$ 6,659,302
First Mortgage Serial Bonds:			
Series One—4%, maturing $500,000 semi-annually from May 1, 1942 to November 1, 1951, inclusive		$10,000,000	
Series Two—3% to November 1, 1941 and 4% thereafter, maturing $500,000 semi-annually from May 1, 1952 to November 1, 1955, inclusive		4,000,000	14,000,000
Reserves:			
For loss on subleases		$ 1,175,659	
For contingent prior years' taxes		826,869	2,002,528
Capital Stock and Surplus:			
Prior preferred stock—			
Authorized 15,000 shares of $100 par value; entitled to 7% cumulative dividends; redeemable at $120 per share and accrued dividends.			
Issued and outstanding 8,965 shares		$ 896,500	
6% cumulative preferred stock—			
Authorized 296,190 shares of $100 par value; redeemable, if no prior preferred stock is outstanding, at $110 per share and accrued dividends; convertible until January 1, 1947 at the option of the holder at the rate of three shares of common stock for each share of preferred stock.			
Issued and outstanding 287,225 shares.		28,722,500	
Common stock—			
Authorized 4,000,000 shares of no par value, of which 888,570 shares are reserved for conversion of 6% cumulative preferred stock and 180,000 shares are reserved for sale to officers and employees.			
Issued 1,659,335 shares at stated value		15,396,675	
Paid-in surplus		5,001,899	
Earned surplus, of which $226,774 is restricted by reason of purchase of treasury stock		6,869,301	
Capital stock and surplus before deducting treasury stock		$56,886,875	
Less—Treasury common stock, 15,278 shares, at cost		226,774	
Capital stock and surplus, net			56,660,101
			$79,321,931

NOTE No. 2.—Dividends in arrears on prior preferred stock, $5.25 per share, and on 6% cumulative preferred stock, $4.50 per share, aggregate $1,339,579.

Statements of Profit and Loss and Surplus

For the Year Ended December 31, 1938

Profit and Loss

NET SALES TO CUSTOMERS		$79,648,166
COST OF SALES AND OPERATING EXPENSES		75,569,902
Net profit from merchandising operations		$ 4,078,264
PROFIT FROM REAL ESTATE OPERATIONS:		
Rental income from tenants	$ 2,631,750	
Operating expenses, less rentals charged to merchandising divisions	2,421,782	209,968
Net profit from operations before interest and special charges		$ 4,288,232
INTEREST CHARGES, ETC.:		
Interest on first mortgage serial bonds	$ 520,000	
Interest on serial notes, etc.	92,257	
Provision for amount due to Estate of James O. McKinsey under option exercised in 1938	33,737	
Provision for Federal income tax (see Note 3)	150,000	795,994
Net profit for the year		$ 3,492,238

NOTES:

(1) Provisions for depreciation of buildings and equipment and amortization of leaseholds included as deductions amount to $2,349,332.

(2) Provisions for real estate, personal property, social security, franchise, occupation and other taxes, included as deductions amount to $3,945,620.

(3) Certain liquidation losses charged against reserves in 1938 are deductible for income tax purposes; such deductions reduce by approximately $400,000 the required provision for Federal income taxes for 1938.

Earned Surplus

BALANCE AT DECEMBER 31, 1937		$ 3,563,837
ADD—		
Net profit for the year 1938		3,492,238
Balance of reserve for loss on disposition of properties, inventories, etc. in connection with reorganization of Manufacturing Division, restored to surplus		259,752
		$ 7,315,827
DEDUCT—		
Cash dividends paid (to March 31, 1938)—		
Prior preferred stock ($1.75 per share)	$ 15,689	
Cumulative preferred stock ($1.50 per share)	430,837	446,526
BALANCE AT DECEMBER 31, 1938		$ 6,869,301

Paid-In Surplus

No changes were recorded during the year in this account.

Statements of Reserve Accounts
For the Year Ended December 31, 1938

Reserve for Possible Loss on Contemplated Disposition of Properties, Future Inventory Losses, etc., in Connection with Reorganization of Manufacturing Division

Balance December 31, 1937		$ 3,569,682
Deduct—		
Loss on disposition of inventories and properties in reorganization of Manufacturing Division (including losses of subsidiary corporations liquidated during the year)	$ 2,423,524	
Amount transferred to reserve for loss on subleases, representing estimated future losses to be sustained under subleases executed in connection with above reorganization transactions, etc.	886,406	
Balance of reserve restored to surplus	259,752	3,569,682
Balance December 31, 1938		$ —

Reserve for Loss on Subleases

Balance December 31, 1937	$ 432,230
Deduct—Excess of rentals, taxes, insurance, etc. paid on subleased properties during 1938 over rentals received	142,977
	$ 289,253
Add—Amount transferred from above reserve	886,406
Balance December 31, 1938	$ 1,175,659

ARTHUR ANDERSEN & CO.

135 SOUTH LA SALLE STREET
CHICAGO

To the Board of Directors,
Marshall Field & Company:

We have made an examination of the balance sheet of MARSHALL FIELD & COMPANY (an Illinois corporation), as at December 31, 1938, and of the statements of profit and loss, surplus and reserves for the year ended that date. In connection therewith, we examined or tested accounting records of the company and other supporting evidence, and obtained information and explanations from officers and employees of the company; we also made a general review of the accounting methods and of the operating and income accounts for the year, but we did not make a detailed audit of the transactions.

In our opinion, based upon such examination, the accompanying balance sheet and related statements of profit and loss, surplus and reserves fairly present, in accordance with accepted principles of accounting consistently maintained by the company during the year under review, the financial position of the company at December 31, 1938, and the results of its operations for the year ended that date.

ARTHUR ANDERSEN & Co.

Chicago, Illinois,
February 2, 1939.